No. 22598

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

REPUBLIC NATIONAL LIFE INSURANCE COMPANY,
Appellant,

vs.

HAMILTON LIFE INSURANCE COMPANY OF NEW YORK and FINANCIAL SECURITY LIFE INSURANCE COMPANY,
Appellees.

BRIEF OF APPELLEE HAMILTON LIFE INSURANCE COMPANY OF NEW YORK

LEWIS ROCA BEAUCHAMP & LINTON

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COMPANY OF NEW YORK

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STATEMENT OF ISSUES

Hamilton Life Insurance Company of New York (hereafter "Hamilton Life") objects to the inclusion of Issue II at page 5 of the brief of Republic National Life Insurance Company (hereafter "Republic National"): "Whether the District Court erred in failing to pass upon the facts of whether there was a written arbitration agreement between the parties and arbitrable issues." In its order of February 15, 1968, the Arizona District Court stated: ". . . this Court being satisfied that on the face of the pleadings there is a written contract involving commerce with

disputed issues under the contract that come within the scope of the arbitration clause contained in the contract . . . ." (R. 101).

Hamilton Life believes that the issues properly before the Court on this appeal are the following:

1. Whether the Arizona District Court properly referred to the New York District Court the question of whether the McCarran Act renders unenforceable the parties' written agreement to arbitrate.

2. Whether the Arizona District Court acted properly under its inherent power to grant a stay of proceedings in that Court pending conclusion of the New York arbitration proceedings.

3. In the alternative only, whether the McCarran Act precludes application of the Federal Arbitration Act to insurance companies.

STATEMENT OF THE CASE

This is an appeal from an order of the United States District Court for the District of Arizona granting a motion of defendant Hamilton Life to stay further proceedings in the Arizona Court pending a decision on Hamilton Life's petition for arbitration in the United States District Court for the Southern District of New York, and from an order of the Arizona court denying plaintiff's motion for rehearing. The District Court had jurisdiction under 28 U.S.C. Sec. 1332. The United States Court of Appeals for the Ninth Circuit has jurisdiction of this appeal under 28 U.S.C. Sec. 1292. *Hudson Lumber Co. v. United States Plywood Corp.,* 181 F.2d 929 (9th Cir. 1950).

On September 21, 1965, plaintiff Republic National and defendant Hamilton Life entered into a reinsurance agreement (Exhibit "A" to the complaint), Article XII of which provided for arbitration in New York of all differences and disputes arising under the agreement.* Differences and disputes did arise. On

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* The allegations of a parol agreement do not find support in the record, and Hamilton Life objects to the references to such an agreement at pp. 2-3 of Republic National's brief.

July 13, 1967, Republic National filed what purported to be an interpleader action in the United States District Court in Texas against this defendant and others. On October 23, 1967, the Texas court dismissed that action for lack of jurisdiction. Republic National appealed, but abandoned its appeal (Einhorn Affidavit, R. 30). Meanwhile, on July 27, 1967, Hamilton Life made a formal demand for arbitration as provided in the agreement. Without responding to that demand, Republic National instituted this action in Arizona, filing with its complaint a notice of refusal to arbitrate.* However, Hamilton Life served a notice of appointment of arbitrator upon plaintiff on November 14, 1967 (R. 30), and on December 11, 1967, filed a petition to compel arbitration in United States District Court for the Southern District of New York (R. 32). That proceeding was brought under 9 U.S.C. Sec. 4. On July 30, 1968, Hamilton Life's motion to compel arbitration was granted by the New York court, which found that Republic National "has subjected Hamilton to a barrage of court proceedings in an effort to obtain judicial relief," instead of proceeding to arbitration. The opinion granting arbitration is set out in Addendum C to this brief.

Incidental to the New York action, Hamilton Life filed a motion in the United States District Court for the District of Arizona for a stay of proceedings in that court pending the arbitration sought in New York (R. 10). That motion was granted (R. 83), and plaintiff's motion for rehearing was denied (R. 101). Plaintiff thereupon filed this appeal (R. 103). This Court granted an ex parte stay of the orders of the Arizona court for a few days, then vacated its stay. Republic National thereupon filed with the Clerk of the Supreme Court of the United States a motion to stay the orders of the Arizona Court pending this appeal, and Mr.

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* Hamilton Life's demand for arbitration and Republic National's notice of refusal to arbitrate, though on file with the District Court, have apparently not been transmitted to this Court. They are set out in Addendum B to this brief.

Justice Black sumarily denied Republic National's motion.* Republic National then filed its opening brief with this Court.

ARGUMENT

I. *Introduction.*

Hamilton Life and Republic National entered into a written agreement to arbitrate, and Hamilton Life has brought proceedings for that purpose in the forum of arbitration, New York. The matter proceeded in two jurisdictions, since Republic National had brought suit against Hamilton Life in Arizona. In both courts, Republic National has argued that the McCarran Act renders unenforceable the arbitration agreement of the parties. The essential question before this Court is which District Court should rule upon Republic National's alleged defense to the arbitration proceedings. Hamilton Life contends that the appropriate forum for this defense is the United States District Court of the Southern District of New York, where Hamilton Life has brought an action to enforce arbitration. Hamilton Life further argues that even were the matter to be decided by the Arizona court, Republic National's McCarran Act argument is without substance.

II. *The Arizona District Court Properly Referred to the New York District Court the Question of Whether the McCarran Act Precludes Enforcement of the Parties' Written Agreement to Arbitrate.*

Republic National argues that under the McCarran Act, Texas law prohibits the enforceability of the parties' agreement to arbitrate. The question before this Court is whether that determination may be made by the court in which arbitration has been sought by Hamilton Life (the United States District Court for the Southern District of New York), or must be made by the court in which Republic National seeks a declaration that it is not liable to Hamilton Life, or for a determination of the

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* Letter from Clerk of United States Supreme Court to John P. Frank, March 12, 1968.

extent of such liability (the United States District Court for the District of Arizona).*

The agreement of the parties provides for arbitration of disputes in the State of New York. The Federal Arbitration Act, relevant provisions of which are set out in Addendum A to this brief, makes arbitration agreements of this sort "valid, irrevocable and enforceable." 9 U.S.C. Sec. 2. The court in which a suit is pending which involves issues referable to arbitration "shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement . . ." 9 U.S.C. Sec. 3. If there is a failure to arbitrate, the party aggrieved may apply for a court order to compel arbitration. 9 U.S.C. Sec. 4. That is precisely what has been done by Hamilton Life in this case. The arbitration jurisdictionally must then go forward in the district in which the application is made, by virtue of the express language of the statute and the cases. *Continental Grain Co. v. Dant & Russell, Inc.,* 118 F.2d 967 (9th Cir. 1941). Where, as here, the arbitration agreement requires arbitration in the State of New York, no other jurisdiction can direct the arbitration there except a New York Court. *China Union Lines, Ltd. v. Steamship Co.,* 136 F. Supp. 597 (S.D.N.Y. 1955). Common sense indicates that all alleged defenses against Hamilton Life's right to secure arbitration of the disputes should be brought in the court which has jurisdiction over the arbitration proceedings, the Southern District of New York, and not elsewhere. The precise legal question is whether the federal arbitration statutes and the cases accord with this approach.

The answer is yes. The motion in the Arizona court for a stay of proceedings under Sec. 3 of the Federal Arbitration Act was not a proper occasion for ruling upon disputed matters. In *Tepper Realty Co. v. Mosaic Tile Co.,* 259 F. Supp. 688 (S.D.N.Y.

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* The New York Court has already made this determination, holding that the arbitration agreement is enforceable. See Addendum C.

1966), the court held that the question of who were the parties to the arbitration agreement was a matter properly to be heard under a motion to compel arbitration under 9 U.S.C. Sec. 4, rather than a motion to stay proceedings under 9 U.S.C. Sec. 3. The court stated:

> "Section 3 makes no provision for preliminary trials of issues which have been, or may be, raised in an answer but commands a stay if the claim asserted in the complaint is one which is subject to the arbitration agreement. There can be no question that on its face the claim alleged here is subject to, and within the ambit of, the arbitration agreement. That is enough to satisfy the requirements for a stay under §3." 259 F. Supp. at 693.

This conclusion is reinforced by the rule that the allegations of the party moving for a stay of proceedings must be accepted as true. *In re Pahlberg,* 43 F. Supp. 761, 764 (S.D.N.Y.), *appeal dismissed,* 131 F.2d 968 (2d Cir. 1942). This rule indicates the courts' unwillingness to enter into determinations of questions of fact and law on a motion for a stay of proceedings under 9 U.S.C. Sec. 3.*

The issues raised by Republic National in the Arizona court constitute a challenge to the jurisdiction of the New York court under the Federal Arbitration Act. But clearly the New York court, the only court which can render a decision on the merits of the arbitration proceedings, is entitled to make its own determination of its jurisdiction. As was held in *McBeath v. Inter-American Citizens for Decency Comm.,* 374 F.2d 359 (5th Cir. 1967), *cert. denied,* 389 U.S. 896, 88 S. Ct. 216, 19 L. Ed. 2d 213 (1967):

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* See also *Lesser Towers, Inc. v. Roscoe-Ajax Constr. Co.,* 258 F. Supp. 1005 (S.D. Cal. 1966). This case is in part immaterial because it involves questions of removal from a state to a federal court, and a matter of timeliness; but it is also suggestive for various of the dicta which it contains. We read the case to hold that where there is a question of what law is to be applied in interpreting a contract, the court which has assumed jurisdiction of the arbitration proceeding should dispose of all the legal questions. 258 F. Supp. at 1012.

"Undoubtedly, under Rule 12(d) of the Federal Rules of Civil Procedure a court may determine the prerequisites to jurisdiction in advance of the trial on the merits. However, where the factual and jurisdictional issues are completely intermeshed the jurisdictional issues should be referred to the merits, for it is impossible to decide the one without the other." 374 F.2d at 362-63.

The Arizona District Court did decide in the present case that, on the face of the pleadings, the claim was subject to the parties' arbitration agreement. Having made that determination, the court properly held that Republic National's alleged defenses against arbitration should be decided by the only court having jurisdiction of the arbitration—the United States District Court for the Southern District of New York.

III. *The Arizona District Court Acted Properly Under its Inherent Power to Grant a Stay.*

Wholly apart from the provisions of the Federal Arbitration Act relating to the granting of a stay of proceedings pending arbitration, the Arizona District Court had inherent power to grant such a stay. This inherent power was relied upon in granting a stay of court proceedings pending arbitration in *Nederlandse Erts-Tankersmaatschappij v. Isbrandtsen Co.,* 339 F.2d 440 (2d Cir. 1964). A similar result was reached with respect to an issue allegedly outside the scope of the arbitration agreement in *Tepper Realty Co. v. Mosaic Tile Co., supra.*

Under these decisions, the court, in considering whether the motion for a stay should be granted, need consider only whether the stay will effectively bring about a resolution of the dispute between the parties, and ease the crowding of court dockets. That is surely the case here. Arbitration, if allowed to proceed in New York, will dispose of many issues in the Arizona case, and will

carry out the agreement of the parties as to the manner of the settlement of their disputes.*

Republic National argues, at pp. 23-24 of its brief, that the decision of the District Court was based upon the Federal Arbitration Act, rather than the court's inherent power to grant a stay. However, the decision of the District Court must be upheld if there is *any* proper basis for the decision, even if the specific rationale used by the court was inappropriate. *J. E. Riley Inv. Co. v. Commissioner,* 311 U.S. 55, 61 S. Ct. 95, 85 L. Ed. 36 (1940); *SEC v. Chenery Corp.,* 318 U.S. 80, 63 S. Ct. 454, 87 L. Ed. 626 (1943).

Because the Arizona District Court had discretion to grant a stay even if it accepted all of Republic National's arguments, its decision should not be disturbed on appeal.

Republic National apparently concedes the inherent power of a court to grant a stay of its own proceedings pending arbitration in another jurisdiction. But Republic National argues, beginning at p. 24 of its brief, that the exercise of such power would have been inappropriate in the present case. Republic National bases its argument on the decision in *Kerotest Mfg. Co. v. C-O-Two Fire Equip. Co.,* 342 U.S. 180, 72 S. Ct. 219, 96 L. Ed. 200 (1952). But that decision, and the line of cases following it, are simply inappropriate to the present lawsuit. In that case, one party sought a declaratory judgment in Delaware, against a party that had instituted a lawsuit in Illinois for an injunction. The Court of Appeals held that the Delaware litigation should be stayed pending determination of the earlier lawsuit filed in Illinois. The court found that nothing would be decided in Delaware that could not also be decided in Illinois, while substantial issues

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* A stay granted under the inherent powers of the court, without reference to the Federal Arbitration Act, makes the entire McCarran Act argument of Republic National wholly irrelevant to the Arizona proceedings, for that court then does not apply any federal statutes. Republic National could, of course, still raise the McCarran Act issue as a defense against arbitration in the New York court, as it has done.

would remain to be decided in the Illinois court regardless of the outcome of the Delaware action. The Court of Appeals therefore held that the Delaware action should be stayed, an exercise of discretion which the United States Supreme Court declined to upset. The *Kerotest* situation is wholly distinguishable from the present case, in which the Arizona court has no power to enforce the arbitration agreement of the parties, and where the successful completion of arbitration in New York may well dispose of virtually all issues before the Arizona court. The very considerations operative in the *Kerotest* decision thus indicate that the stay of Arizona proceedings pending the completion of arbitration in New York was proper.

This is particularly true where a narrow question such as the effect of the McCarran Act on arbitration proceedings is before the tribunal which can best deal with it—here the court which can enforce arbitration. See, for example, *Humboldt Placer Mining Co. v. Best,* 185 F. Supp. 290 (N.D. Cal. 1960), in which the United States filed condemnation suits in the California District Court. The defendants then instituted contest proceedings before the Bureau of Land Management. The plaintiff brought a complaint for an injunction against those proceedings. A temporary restraining order was granted, and defendants asked the court to vacate that order. The court held:

> [W]here a court has jurisdiction of an entire controversy, it may wait until a court or tribunal of more limited jurisdiction adjudicates the issues peculiarly within its competency, and then give binding effect to the decision of such court or tribunal . . ." 185 F. Supp. at 291-92.

This judgment was vacated, 293 F.2d 553 (9th Cir. 1961), but that decision was reversed, 371 U.S. 334, 83 S. Ct. 379, 9 L. Ed. 2d 350 (1963). See also *Lowry & Co. v. S.S. Nadir,* 223 F. Supp. 871 (S.D.N.Y. 1963), staying a court action until arbitration is completed abroad.

The Arizona court clearly had discretion to grant the stay, and its exercise of discretion should not be overturned by this Court.

IV. *The McCarran Act does not Preclude Application of the Federal Arbitration Act to Reinsurance Agreements Between Insurance Companies.*

Plaintiff argues that the McCarran-Ferguson Act (15 U.S.C. Sec. 1011 et seq.) precludes the application of the Federal Arbitration Act to disputes between insurance companies, for such application would invalidate, impair or supersede applicable Texas law. Relevant provisions of that Act are set out in Addendum A. Sec. 1012(b) provides:

> "No act of Congress shall be construed to invalidate, impair or supersede any law enacted by any state for the purpose of regulating the business of insurance . . . unless such act specifically relates to the business of insurance . . . ."

The Arizona court did not consider the merits of Republic National's argument, holding that the McCarran Act issue was properly to be considered by the New York District Court, rather than the Arizona District Court. As argued above, the stay of the Arizona proceedings pending arbitration was justifiable under the court's inherent power to grant a stay, and the decision of the lower court should be upheld for that reason, completely irrespective of any considerations of the McCarran Act and the Federal Arbitration Act. But if the Court does feel that this is a proper occasion for considering the McCarran Act issues raised by Republic National, Hamilton Life urges that the McCarran Act does not preclude enforcement of an arbitration agreement entered into by insurance companies.

A. *The Relevant State Law, that of New York, Would Not be Invalidated, Impaired or Superseded by Application of the Federal Arbitration Act.*

As the United States District Court for the Southern District of New York has held in this case, New York law would be applicable to this transaction, because almost all of the significant contacts of the transactions were with New York. The ultimate insureds reside in that state, and it was agreed that arbitration

would take place there. (See Addendum C). Arbitration relates to the law of remedies. *Red Cross Line v. Atlantic Fruit Co.,* 264 U.S. 109, 44 S. Ct. 274, 68 L. Ed. 582 (1924); *Marine Transit Corp. v. Dreyfus,* 284 U.S. 263, 52 S. Ct. 166, 76 L. Ed. 282 (1932). Where the parties agree to arbitration in a particular state, their agreement is governed by the arbitration law of that state. As the Court of Civil Appeals of Texas stated in *Brownwood Mfg. Co. v. Tanenbaum Textile Co.,* 404 S.W.2d 106 (1966):

> "When appellants entered into these written contracts providing for arbitration in New York, they were charged with notice of the New York laws pertaining to arbitration and consented to be bound thereby." 404 S.W.2d at 109.

See also *Carrington, The 1965 General Arbitration Statute of Texas,* 20: 21 Sw. L. J. 21, 52 (1966):

> "[T]he mere incorporation of an expression indicating that the parties expect or provide that the arbitration shall be held in New York, may be the equivalent of an express agreement that the provisions of the statutes of that state shall apply."

Application of New York law is also supported by the rule that parties to an agreement must be deemed to have intended a valid act. Thus, even if Texas laws do prohibit arbitration, as Republic National argues, the court would not apply Texas law, which would render the parties' agreement invalid, but would rather apply New York law, which would give effect to the agreement to arbitrate. See *Grace v. Orkin Exterminating Co.,* 255 S.W.2d 279 (Tex. Civ. App. 1953):

> "It is ordinarily to be implied that parties who have purportedly entered into a contract intended the agreement to be legally effective, and this implication has been frequently resorted to in settling questions of conflicts of laws . . . . We conclude that the parties to the written contract intended their written agreement to be given such legal effect and validity as could be given it, and as an incident of this intention should be taken to have necessarily intended that validity be determined by the system of law which would give effect to the agreement rather

than by a system which would hold it invalid." 255 S.W. at 292-93.

By agreeing to arbitration in New York, the parties have agreed to the applicability of New York laws, rather than Texas laws relating to arbitration. The argument of Republic National, that application of the Federal Arbitration Act would invalidate, impair or supersede Texas laws relating to arbitration is therefore inappropriate; the relevant question is whether the application of the Federal Arbitration Act would impair, invalidate or supersede relevant provisions of New York law.

Application of the Federal Arbitration Act would not have an effect upon New York law prohibited by the McCarran Act. The United States District Court for the Southern District of New York has so held, in the opinion set forth in Addendum C, pp. 37-39. We incorporate that decision herein, and ask that the Court weigh and consider the cases and arguments relied upon by the New York court. That court rejected the argument raised by Republic National, at page 18 of its brief, that under New York law the validity of a contract containing an arbitration clause is to be determined by the courts, not by the arbitrators, unlike proceedings under the Federal Arbitration Act. The New York court held, after examination of the statutes and cases, that New York law was unsettled on the question of who decides whether a contract containing an arbitration clause was induced by fraud, but that regardless of how that question was decided, there would be no conflict with the Federal Arbitration Act so as to bring the McCarran Act into play.

B. *Even if Texas Law Were Relevant, Application of the Federal Arbitration Act Would Not Contradict The McCarran Act.*

This issue, too, has been decided by the United States District Court for the Southern District of New York. Because that court carefully weighed the applicable authorities and arguments, we do not set forth here a repetition of the materials, but instead incorporate the New York decision by reference, and ask that

the Court consider its holding on this issue set forth in Addendum C, pp. 33-35.

CONCLUSION

The parties to this appeal have agreed in writing to arbitrate their disputes and differences. Proceedings to enforce that arbitration agreement are now under way in New York. The arbitration statutes, the cases, and the interests of judicial administration compel Republic National to raise its defenses against arbitration in the jurisdiction where arbitration is sought, rather than in the District of Arizona. The Arizona District Court recognized this, and stayed its own proceedings pending arbitration in New York. If this was not commanded by the cases and statutes, certainly the Arizona Court had discretion to enter such an order, and it should not be disturbed on appeal. Even if it were necessary to confront Republic National's objections to arbitration on the merits, those objections are unsound. There is simply no reasonable basis upon which it can be asserted that the McCarran Act precludes enforcement of the parties' arbitration agreement under the Federal Arbitration Act.

The orders appealed from should be affirmed.

LEWIS ROCA BEAUCHAMP & LINTON

By JOHN P. FRANK
Attorneys for Appellee
Hamilton Life Insurance
Company of New York

August, 1968.

CERTIFICATION

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with the rules.

John P. Frank

ADDENDUM A

UNITED STATES CODE ANNOTATED

TITLE 9

ARBITRATION

Section 2. Validity, irrevocability, and enforcement of agreements to arbitrate

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract. July 30, 1947, c. 392, Section 1, 61 Stat. 669.

Section 3. Stay of proceedings where issue therein referable to arbitration

If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration. July 30, 1947, c. 392, Section 1, 61 Stat. 669.

Section 4. Failure to arbitrate under agreement; petition to United States Court having jurisdiction for order to compel arbitration; notice and service thereof; hearing and determination

A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may

petition any United States district court which, save for such agreement, would have jurisdiction under Title 28, in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement. Five days' notice in writing of such application shall be served upon the party in default. Service thereof shall be made in the manner provided by the Federal Rules of Civil Procedure. The court shall hear the parties, and upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement. The hearing and proceedings, under such agreement, shall be within the district in which the petition for an order directing such arbitration is filed. If the making of the arbitration agreement or the failure, neglect, or refusal to perform the same be in issue, the court shall proceed summarily to the trial thereof. If no jury trial be demanded by the party alleged to be in default, or if the matter in dispute is within admiralty jurisdiction, the court shall hear and determine such issue. Where such an issue is raised, the party alleged to be default may, except in cases of admiralty, on or before the return day of the notice of application, demand a jury trial of such issue, and upon such demand the court shall make an order referring the issue or issues to a jury in the manner provided by the Federal Rules of Civil Procedure, or may specially call a jury for that purpose. If the jury find that no agreement in writing for arbitration was made or that there is no default in proceeding thereunder, the proceeding shall be dismissed. If the jury find that an agreement for arbitration was made in writing and that there is a default in proceeding thereunder, the court shall make an order summarily directing the parties to proceed with the arbitration in accordance with the terms thereof. As amended Sept. 3, 1954, c. 1263, Section 19, 68 Stat. 1233.

TITLE 15
COMMERCE AND TRADE
SECTIONS 1011-1014
THE McCARRAN-FERGUSON ACT

Section 1011. Declaration of policy

Congress declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States. Mar. 9, 1945, c. 20, Sec. 1, 59 Stat. 33.

Section 1012. Regulation by State law, Federal law relating specifically to insurance; applicability of certain Federal laws after June 30, 1948

(a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: Provided, That after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law. Mar. 9, 1945, c. 20, Secs. 2, 59 Stat. 34; July 25, 1947, c. 326, 61 Stat. 448.

ADDENDUM B

DEMAND FOR ARBITRATION

Date: July 27, 1967

TO: Republic National Life Insurance Company
3988 North Central Expressway
Dallas, Texas 75204

PLEASE TAKE NOTICE, under Section 7503, Subdivision (c), of the Civil Practice Law and Rules of the State of New York, that pursuant to the provisions of a contract duly entered into between Republic National Life Insurance Company and Hamilton Life Insurance Company of New York on September 21, 1965, which contract provides as follows:

"ARTICLE XII ARBITRATION

1. All disputes and differences between the two contracting parties upon which an amicable understanding cannot be reached are to be decided by arbitration and the arbitrators shall place a liberal construction upon this agreement free from legal technicalities, for the purpose of carrying out its evident intent.

2. The court of arbitrators, which is to be held in the city where the home office of CEDING COMPANY is domiciled, shall consist of three arbitrators who must be officers of Life insurance companies familiar with the reinsurance business, other than the two parties to this agreement. One of the arbitrators is to be appointed by CEDING COMPANY, the second by REPUBLIC NATIONAL and the third is to be selected by these two representatives before the beginning of the arbitration. Should the two arbitrators be unable to agree upon the choice of a third, the appointment shall be left to the president of the American Life Convention.

3. The arbitrators are not bound by any rules of law. They shall decide by a majority of votes and from their written decision there can be no appeal. The cost of arbitration, including the fees of the arbitrators, shall be borne by the losing party unless the arbitrators shall decide otherwise."

Hamilton Life Insurance Company of New York hereby demands arbitration thereunder.

NATURE OF DISPUTE: On September 21, 1965, a group reinsurance agreement was entered into by Hamilton and Republic National, under which it was agreed that Hamilton would cede to Republic National and Republic National would accept liability for certain group life insurance claims paid by Hamilton, to the extent of 80% thereof. Pursuant to the said reinsurance agreement, Hamilton ceded to Republic National and Republic National accepted certain business under group policies of life insurance. Thereafter, Hamilton paid various claims under the group insurance contracts ceded to and accepted by Republic National and Republic National's share thereof under the above-mentioned reinsurance agreement is $278,023.41. Upon such payment by Hamilton, Republic National became obligated to pay to Hamilton the sum of $278,023.41. Republic National has denied that it is obligated to Hamilton in the said amount or in any amount and has refused to make payment to Hamilton.

CLAIM OR RELIEF SOUGHT: Hamilton seeks an award directing payment to it by Republic National of the sum of $278,023.41.

PLEASE TAKE FURTHER NOTICE, that unless within ten days after service of this Notice of Intention to Arbitrate, you apply to stay the arbitration herein, you shall thereafter be precluded from objecting that a valid agreement was not made or has not been complied with and from asserting in court the bar of a limitation of time.

HEARING LOCALE DEMANDED: New York City.

Yours, etc.,

ARANOW, BRODSKY, BOHLINGER,
EINHORN & DANN

By: /s/ Herbert A. Einhorn
A Member of the Firm

Attorneys for Hamilton Life Insurance
Company of New York
Office and P. O. Address
122 East 42nd Street
New York, New York 10017

212 687-6343

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF ARIZONA

REPUBLIC NATIONAL LIFE INSURANCE COMPANY, Plaintiff, vs. FINANCIAL SECURITY LIFE INSURANCE COMPANY and HAMILTON LIFE INSURANCE COMPANY OF NEW YORK, Defendants.	No. CIV-6501 PHX. NOTICE OF REFUSAL TO ARBITRATE

Republic National Life Insurance Company, Plaintiff in the captioned action, having previously received written demand for arbitration as specified below, relative to such demand states:

I

Petitioner has been served with a "Demand for Arbitration" by attorneys for Hamilton Life Insurance Company, one of the Defendants in this cause. A true and correct copy thereof is attached hereto marked Exhibit "1".

II

That suit in the nature of interpleader was filed in the United States District Court for the Northern District of Texas on July 13, 1967. That on October 23, 1967 said court entered its order dismissing the cause of action to which order Plaintiff gave its notice of appeal within the time period prescribed. Subsequently suit was filed by Plaintiff in the United States District Court for the District of Arizona on November 3, 1967. A true and correct copy of the complaint marked Exhibit "2" is attached hereto and made a part hereof, the same as though set out herein in full. By reason of such suit, exclusive jurisdiction to try all

matters at issue resides in the Court in which the complaint is filed and no demand for arbitration may properly oust the jurisdiction of the court already attached.

III

The reinsurance contract between Republic National Life Insurance Company and Hamilton Life Insurance Company is a Texas contract and must be construed in accordance with the laws of Texas which prohibit arbitration contracts and particularly those pertaining to insurance.

IV

The purported agreement to arbitrate is invalid and illegal on its face for reasons that are self-apparent.

V

Further, Republic National Life Insurance Company has alleged in its complaint in this action that the contract referred to in the demand for arbitration is itself now invalid and unenforceable and revoked or subject to revocation under the circumstances stated in the complaint, all of which under the law precludes arbitration of the issues and controversies referred to in the demand for arbitration.

VI

The controversies stated in the complaint arise between Republic National Life Insurance Company, Hamilton Life Insurance Company of New York, and Financial Security Life Insurance Company; and no agreement exists making disputes arising between these three parties subject to arbitration.

WHEREFORE, Republic National Life Insurance Company respectfully refuses to honor the demand for arbitration previously served upon it as stated above, and requests that the court make its order directing the time and method of service of this notice upon the Defendants in this cause who have not appeared to date and are not yet in default, together with such

other and further orders relative to the matters stated as are appropriate in the law or equity.

Respectfully submitted,

CARSON MESSINGER ELLIOTT
& RAGAN

By ROBERT W. HOLLAND
1400 Guaranty Bank Building
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ADDENDUM C

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

HAMILTON LIFE INSURANCE COMPANY OF NEW YORK, Petitioner, - against - REPUBLIC NATIONAL LIFE INSURANCE COMPANY, Respondent.	67 Civ. 4855

OPINION

APPEARANCES:

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ROBERT W. HOLLAND
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HERLANDS, District Judge:

Novel and important questions of federal-state relations in accommodating the Federal Arbitration Act, 9 U.S.C. § 1 et seq. with the McCarran-Ferguson Insurance Regulation Act,

15 U.S.C. § 1011 et seq. are raised by the petitioner's motion and the respondent's cross-motion.

Petitioner Hamilton Life Insurance Company of New York (Hamilton), moves for an order, pursuant to 9 U.S.C. § 4[1] (the Federal Arbitration Act) directing the respondent, Republic National Life Insurance Company (Republic), to proceed to arbitration. Republic has cross-moved, pursuant to Fed. R. Civ. P. 12(b), to dismiss the petition on the following three grounds:

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[1] 9 U.S.C. § 4 provides:

"§ 4. Failure to arbitrate under agreement; petition to United States Court having jurisdiction for order to compel arbitration; notice and service thereof; hearing and determination.

A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court which, save for such agreement, would have jurisdiction under Title 28, in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement. Five days' notice in writing of such application shall be served upon the party in default. Service thereof shall be made in the manner provided by the Federal Rules of Civil Procedure. The court shall hear the parties, and upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement. The hearing and proceedings, under such agreement, shall be within the district in which the petition for an order directing such arbitration is filed. If the making of the arbitration agreement or the failure, neglect, or refusal to perform the same be in issue, the court shall proceed summarily to the trial thereof. If no jury trial be demanded by the party alleged to be in default, or if the matter in dispute is within admiralty jurisdiction, the court shall hear and determine such issue. Where such an issue is raised, the party alleged to be in default, may, except in cases of admiralty, on or before the return of the notice of application, demand a jury trial of such issue, and upon such demand the court shall make an order referring the issue or issues to a jury in the manner provided by the Federal Rules of Civil Procedure, or may specially call a jury for that purpose. If the jury find that no agreement in writing for arbitration was made or that there is no default in proceeding thereunder, the proceeding shall be dismssed. If the jury find that an agreement for arbitration was made in writing and that there is a default in proceeding thereunder, the court shall make an order summarily directing the parties to proceed with the arbitration in accordance with the terms thereof."

(1) that the Court lacks subject matter jurisdiction; (2) that the Court lacks in personam jurisdiction over Republic; and (3) that Hamilton has failed to join an indispensable party. As alternative relief, Republic seeks a stay of all proceedings pending the determination by the Court of Appeals for the Ninth Circuit of an appeal in a related proceeding.

On September 21, 1965, Republic and Hamilton entered into a group reinsurance agreement. This provided that Republic would reinsure a certain percentage of the risks on group life insurance policies written by Hamilton covering civil service employees in the New York City area. The group reinsurance agreement is contained in a standard form of reinsurance contract furnished by Republic. It was executed in New York City by an officer of Hamilton, who then mailed it to Republic's office in Dallas, Texas for signature. (Affidavit of Robert H. Autenreich, sworn to December 12, 1967, pp. 2-3). After the agreement was executed, additional negotiations occurred. As a result, there was a change in the first year administrative charge on ceded business. This change was made in the original reinsurance agreement, which was first initialed by an officer of Republic in Dallas, Texas and then by an officer of Hamilton in New York City, in October, 1965. (Autenreich Affidavit, p. 3 and Exhibit 1 attached thereto).

The reinsurance agreement contains the following broad arbitration clause:

"ARTICLE XII ARBITRATION

1. All disputes and differences between the two contracting parties upon which an amicable understanding cannot be reached are to be decided by arbitration and the arbitrators shall place a liberal construction upon this agreement free from legal technicalities, for the purpose of carrying out its evident intent.

2. The court of arbitrators, which is to be held in the city where the home office of CEDING COMPANY [Hamilton] is domiciled, shall consist of three arbitrators who must be officers

of Life insurance companies familiar with the reinsurance business, other than the two parties to this agreement. One of the arbitrators is to be appointed by CEDING COMPANY [Hamilton], the second by REPUBLIC NATIONAL and the third is to be selected by these two representatives before the beginning of the arbitration. Should the two arbitrators be unable to agree upon the choice of a third, the appointment shall be left to the president of the American Life Convention.

3. The arbitrators are not bound by any rules of law. They shall decide by a majority of votes and from their written decision there can be no appeal. The cost of arbitration, including the fees of the arbitrators, shall be borne by the losing party unless the arbitrators shall decide otherwise."

Disputes having arisen between the parties, on July 27, 1967 Hamilton served a Demand For Arbitration in New York City on Republic. The Demand For Arbitration recited that Hamilton had paid various claims under group insurance contracts ceded to and accepted by Republic and that by virtue of the reinsurance agreement Republic was obligated to pay Hamilton the sum of $278,023.41. (Exhibit 1 to Affidavit of Herbert A. Einhorn, sworn to December 11, 1967).

On November 14, 1967, Hamilton served a Notice of Appointment of Arbitrator, which also demand that Republic select an arbitrator pursuant to the terms of the reinsurance agreement. (Exhibit 2 to Einhorn Affidavit). Republic, however, has refused to proceed to arbitration. Instead, it has subjected Hamilton to a barrage of court proceedings in an effort to obtain judicial relief.

On July 14, 1967, Republic commenced an action against Hamilton based on the agreement in issue in the United States District Court for the Northern District of Texas. The action was dismissed for lack of jurisdiction on October 23, 1967. Republic appealed from this dismissal on October 30, 1967. On November 17, 1967, Republic voluntarily discontinued its appeal.

On November 3, 1967, Republic commenced a second action against Hamilton, this time in the United States District Court for the District of Arizona. Service of the summons and complaint

in that action was effected on Hamilton on November 20, 1967.

On December 11, 1967, Hamilton filed in this Court a petition to compel arbitration (Hamilton's motion now before the Court), which was brought on for hearing on December 26, 1967 by a notice of motion dated December 12, 1967.

Republic did not file an answer to the petition herein or request an adjourment of the proceedings in this Court. Instead, on December 20, 1967, Republic obtained, *ex parte,* from the United States District Court for the District of Arizona a temporary restraining order prohibiting Hamilton from proceeding before this Court. This order was extended on December 29, 1967. On January 9, 1968, a preliminary injunction against proceeding in this Court was issued in order to afford the United States District Court for the District of Arizona an opportunity to consider the matter fully.

On January 29, 1968 the United States District Court for the District of Arizona quashed its injunction and granted Hamilton a stay of all further proceedings in Arizona pending this Court's determination of the present application for an order directing arbitration.

On February 2, 1968, Republic moved in the Arizona federal district court for a rehearing or for a stay of its order quashing the preliminary injunction against proceeding in this Court pending appeal. On February 15, 1968, the Arizona court adhered to its prior determination but directed that no proceedings take place in the Southern District of New York until February 27, 1968 in order to allow Republic to apply to the Ninth Circuit Court of Appeals for a stay.

On February 19, 1968, Republic applied *ex parte* to said Court of Appeals for a stay. On February 21, 1968, the Ninth Circuit stayed until March 4, 1968 the dissolution of the preliminary injunction against proceeding in the Southern District of New York to allow Hamilton to be heard on Republic's application for a

stay pending appeal. Subsequently, on March 4, 1968, the Ninth Circuit vacated its temporary stay.

On March 7, 1968, Republic applied to the United States Supreme Court for a temporary stay. On March 8, 1968, this application was denied by Mr. Justice Black.

I

Whether the McCarran-Ferguson Insurance Regulation Act, 15 U.S.C. §1011 et seq. (hereinafter the McCarran-Ferguson Act) prevents the petitioner from compelling arbitration of this dispute pursuant to §4 of the Federal Arbitration Act[2] is the threshold and crucial question. For the reasons that follows, this Court answers that question in the negative.

In *United States* v. *South-Eastern Underwriters Ass'n,* 322 U.S. 533 (1944), the Supreme Court decided that the business of insurance was commerce and therefore subject to federal regulatory legislation, specifically the anti-trust laws. *South-Eastern Underwriters* reversed the pre-existing rule that the business of insurance was not commerce and hence subject only to state regulation. See *Paul* v. *Virginia,* 75 U.S. 168 (1868); *New York Life Insurance Co.* v. *Deer Lodge County,* 231 U.S. 495 (1913).

The McCarran-Ferguson Act was enacted in 1945 in order to "allay doubts" that *South-Eastern Underwriters* impaired "the continuing power of the States to tax and regulate the business of insurance." *FTC* v. *Travelers Health Ass'n,* 362 U.S. 293, 299 (1960); *State Board of Insurance* v. *Todd Shipyards Corp.,* 370 U.S. 451, 452 (1962); *Maryland Casualty Co.* v. *Cushing,* 347

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[2] It is uncontroverted that the agreement in issue satisfies the jurisdictional requirements of the Act. Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2, provides that a written arbitration provision "in * * * a contract evidencing a transaction involving commerce * * * shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." The agreement in issue involving interstate transactions between companies of different states is manifestly one "evidencing a transaction involving [interstate] commerce."

U.S. 409, 413 (1954); *Prudential Insurance Co.* v. *Benjamin,* 328 U.S. 408, 429-433 (1946).

The purpose and scope of the statute is summed up in the House Report on the bill:

> "It is not the intention of Congress in the enactment of this legislation to clothe the States with any power to regulate or tax the business of insurance beyond that which they had been held to possess prior to the decision of the United States Supreme Court in the *Southeastern Underwriters Association* case. Briefly, your committee is of the opinion that we should provide for the continued regulation and taxation of insurance by the State, subject always, however, to the limitations set out in the controlling decisions of the Supreme Court . . . which hold, *inter alia,* that a State does not have power to tax contracts of insurance or reinsurance entered into outside its jurisdiction by individuals or corporations resident or domiciled therein covering risks within the State or to regulate such transactions in any way." H.R. Rep. No. 143, 79th Cong., 1st Sess. 3 (1945).

The Congressional policy is enunciated in a prefatory section of the Act stating:

> "Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress should not be contrued to impose any barrier to the regulation or taxation of such business by the several States." 15 U.S.C. §1011.

Section 2(b), 15 U.S.C. §1012(b)—the statutory section central to the resolution of the problem now before the Court—provides:

> "No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided,* That after June 30, 1948, . . . the Sherman Act . . . the Clayton Act and . . . the Federal Trade Commission Act . . . shall be applicable to the business of insurance to the extent that such business is not regulated by State law."

Respondent submits that §2(b) of the McCarran-Ferguson Act exempts the business of insurance from the coverage of all federal statutes which do not specifically state that their provisions are applicable to insurance. Because there is no such specification in the Federal Arbitration Act, respondent argues that that statute is not applicable to this insurance case and, consequently, that there is no subject matter jurisdiction to entertain the petition.

Disputing the basic premises underlying the respondent's position, the petitioner contends that the controlling and precise inquiry is whether the Federal Arbitration Act invalidates, impairs or supersedes any conflicting State law enacted for the purpose of regulating the insurance business. In the petitioner's view the Federal Arbitration Act has no such invalidating, impairing or superseding effect in the instant case; ergo, it is not rendered inapplicable by the McCarran-Ferguson Act. But the petitioner does not stake its case entirely on that proposition.

Assuming *arguendo* that the McCarran-Ferguson Act renders the Federal Arbitration Act inapplicable, the petitioner adopts diversity of citizenship as the predicate for this Court's jurisdiction to compel arbitration pursuant to State law. It is the petitioner's claim that this case is controlled by New York law, under which the parties' agreement to arbitrate is valid and specifically enforceable.

The primary issue to be resolved may be broadly formulated in these terms: to what extent does the McCarran-Ferguson Act limit the operation of federal statutes (such as the Federal Arbitration Act) that do not by their terms specifically apply to the business of insurance? The plain and unambiguous statutory language is persuasive evidence that the McCarran-Ferguson Act was not intended to preclude the application of these federal statutes to insurance *unless* they invalidate, impair or supersede applicable State legislation regulating the business of insurance. However, in reaching this conclusion, the Court does more than simply follow the route of statutory language; it seeks to effectuate the

Act's fundamental objective and dominant intention. Judge Learned Hand's celebrated dictum bears repetition: "it is one of the surest indexes of a mature and developed jurisprudence not to make a fortress out of the dictionary; but to remember that statutes always have some purpose or object to accomplish whose sympathetic and imaginative discovery is the surest guide to their meaning." *Cabell* v. *Markham,* 148 F. 2d 737, 739 (2d Cir.), *aff'd* 326 U.S. 404 (1945).

The primary legislative purpose of the McCarran-Ferguson Act was to reaffirm the States' power to regulate insurance (subject to constitutional limitations) and to ensure that state regulatory schemes would not be impaired and overriden except by specific and explicit Congressional enactments. There is no discernible evidence of a legislative intention that, in the absence of conflicting state regulatory legislation, federal statutes (such as the Federal Arbitration Act) would be inapplicable to the business of insurance. This view is brought into sharp focus by decisions interpreting the McCarran-Ferguson Act that have upheld federal law despite conflicting state statutes. *Maryland Casualty Co.* v. *Cushing, supra,* 347 U.S. at 412-413 (Federal Maritime Law—"The question whether application of the [Louisiana] direct action statute conflicts with federal maritime law is not touched by the *South-Eastern Underwriters* case. In the face of this unequivocal expression of congressional meaning, the statute cannot be read as doing something that Congress has told us it was not intended to do. The McCarran Act is not relevant here."); *Sears Roebuck and Co.* v. *All States Life Insurance Co.,* 246 F. 2d 161, 172 (5th Cir. 1957) (Lanham Act—"There is nothing in the McCarran Act that limits the right of the owner of a trade or service name to seek redress in the federal courts merely because the approval of the name of the infringing insurance company is part of the duties of the state board."); *Zachman* v. *Erwin,* 186 F. Supp. 691, 694 (S.D.Tex. 1960) (Securities Act of 1933—"That statute [the McCarran-Ferguson Act] does not preclude application of the Securities Act to the insurance business since there is no indication

that it invalidates, impairs or supersedes any law of the State of Texas regulating the insurance business.").

SEC v. *National Securities Inc.,* 387 F.2d 25 (9th Cir. 1967), *affirming,* 252 F. Supp. 623 (D.Ariz. 1966), upon which respondent principally relies, does not dictate a contrary result. In that case, the Securities and Exchange Commission sought to invalidate the merger of two stock life insurance companies on the ground that the anti-fraud provisions of the Securities Exchange Act of 1934 were violated. The District Court merely held that application of the Federal Act "would at least 'impair', if not 'invalidate' or 'supersede'" an Arizona statute enacted for the purpose of regulating the business of insurance, which contains the specific requirement that any proposed merger of insurance companies must be approved by the state director of insurance. (252 F. Supp. at 626). The Court of Appeals noted that the State of Arizona had "affirmatively asserted its power to regulate the merger of insurance companies" (387 F.2d at 31) and that the legislative history of the 1964 amendments to the Securities Acts indicate that the States were to "be given an opportunity to demonstrate their ability to effectively protect the investors as well as the policyholders." (1964 U.S. Code Cong. & Admin. News, p. 3022, quoted in 387 F.2d at 31, n. 3). The Court of Appeals, therefore, affirmed the District Court's holding that application of the Securities Exchange Act of 1934 would impair, invalidate or supersede the Arizona law. (387 F.2d at 32). The Court did not hold that the Securities Exchange Act of 1934 was inapplicable for the reason that it does not contain a provision making it applicable to insurance. What National Securities, Inc. did hold was that the federal statute did not govern because it impaired a detailed state regulatory scheme specifically and directly aimed at the insurance business.

Next to be considered is the question whether there is any State law enacted for the purpose of regulating insurance which would be invalidated, impaired or superseded if the Federal Ar-

bitration Act is applied to the present case. The only two States having an interest in the present controversy are Texas and New York. Respondent asserts that Article 224 of the present Texas Arbitration Statute is in direct conflict with the Federal Arbitration Act. This Texas provision renders enforceable written agreements to arbitrate future as well as existing disputes put provides that "none of the provisions of this Act shall apply to . . . any contract of insurance or any controversy thereunder." *10 Vernon's Civil Stats.* Art. 224 (1967 Supp.). However, this provision is applicable only to arbitration agreements made after January 1, 1966 and, therefore, would not apply to the instant agreement, which was executed in September, 1965. Id. Art. 238-3 (1967 Supp.). Furthermore, the agreement in question is a contract of reinsurance between two insurance companies, not a standard insurance contract; and the present statute was enacted to protect Texas insureds from being forced to accept insurance policies—particularly "uninsured motorist" policies—containing arbitration clauses. See, Note 44 *Texas L. Rev.* 372, 373 (1965); P. Carrington, *The 1965 General Arbitration Statute of Texas,* 20 *Southwestern L. J.* 21, 38 (1966).

The Texas General Arbitration Act in force at the time the agreement in issue was executed provides that, while agreements to arbitrate existing controversies would be enforced by the courts of Texas, agreements to arbitrate future disputes would not be judicially enforced. *10 Vernon's Civil Stats. Arts. 224-238* (1959 ed.).

Furthermore, this statute is not a "law enacted by any State for the purpose of regulating the business of insurance" within the meaning of § 2(b) of the McCarran-Ferguson Act. The Texas statute is a codification of an old common-law rule, whose purpose was not to regulate the insurance business but rather to preserve the jurisdiction of the courts. See, Dougherty and Graf, *Should Texas Revise Its Arbitration Statutes?,* 41 *Texas L. Rev.* 229 (1962).

Another salient aspect of interpretation is illuminated by those cases which, in construing the proviso to § 2(b) of the McCarran-Ferguson Act, have held that State "regulation" means regulation by the State within whose borders the activity in question has its operative force. In *FTC* v. *Travelers Health Ass'n,* 362 U.S. 293, 300, 301 (1960), the Supreme Court pointedly stated:

> ". . . [I]t is clear that Congress viewed state regulation of insurance solely in terms of regulation by the law of the State where occurred the activity sought to be regulated. There was no indication of any thought that a State could regulate activities carried on beyond its own borders.
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> * * *
>
> The three Senate conferees, Senators McCarran, O'Mahoney and Ferguson, repeatedly emphasized that the provision did not authorize state regulation of extraterritorial activities."

Accord: *United States* v. *Chicago Title and Trust Co.,* 242 F. Supp. 56, 60 (N.D. Ill. 1965) ("The Supreme Court decisions would also indicate the inability of the states to affect matters extraterritorially.").

There is no discernible reason why State "regulation" should be defined differently in § 2(b) of the McCarran-Ferguson Act itself. The legislative history of § 2(b) strongly substantiates the proposition that a State is not empowered to regulate interstate insurance practices which have their situs outside its borders. See H.R. Rep. No. 143, 79th Cong., 1st Sess. 3 (1945). It is this Court's opinion that the agreement herein between the petitioner, a New York corporation and the respondent, a Texas corporation, provides for arbitration in New York City of disputes arising under a contract of reinsurance on group life insurance policies written on New York municipal employees; and that application of the Texas statute to prohibit the submission of this extraterritorial dispute to arbitration in New York City would not be "regulation" within the meaning of § 2(b) of the McCarran-Ferguson Act.

Traditional conflict of laws rules also support the Court's foregoing conclusion. If the Federal Arbitration Act were not applicable to the present case, this Court would have jurisdiction by virtue of diversity of citizenship[3] to decide this case under State law. *Metro Industrial Painting Corp.* v. *Terminal Construction Co.,* 287 F.2d 382, 388, N.3 (2d Cir.) (Lumbard, C.J., concurring), *cert. denied,* 368 U.S. 817 (1961); *Sinva, Inc.* v. *Merrill, Lynch, Pierce, Fenner & Smith, Inc.,* 253 F.Supp. 359, 363 (S.D.N.Y. 1966); *Formigli Corp.* v. *Alcar Builders Inc.,* 329 F.2d 79, 81 (3d Cir. 1964); *O'Meara* v. *Texas Gas Transmission Corp.,* 230 F.Supp. 788, 790 (N.D.Ill. 1964); *Cook* v. *Kuljian Corp.,* 201 F.Supp. 531, 535 (E.D.Pa. 1962). Cf. *Boston & Maine Corp.* v. *Chicago, B & Q RR Co.,* 381 F.2d 365 (2d Cir. 1967).

Under *Klaxon Co.* v. *Stentor Elec. Mfg. Co.,* 313 U.S. 487 (1941), this Court would apply New York choice-of-law rules to determine whether Texas or New York law is applicable to the instant dispute. For conflicts purposes, New York treats arbitration as being part of its "law of remedies" and, therefore, the law of the forum (New York) would govern. *Matter of Gantt,* 297 N.Y. 433, 438-439 (1948); *Metro Industrial Painting Corp.*

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[3] Respondent's contention that, absent the Federal Arbitration Act, this Court lacks subject matter jurisdiction is rejected. The Federal Arbitration Acts does not create an independent basis for federal jurisdiction. Apart from the requirements of the Act, diversity of citizenship or a federal question is requisite for federal jurisdiction. *Robert Lawrence Co. v. Devonshire Fabrics, Inc.,* 271 F.2d 402, 408 (2d Cir. 1959), *cert. dismissed,* 364 U.S. 801 (1960); *Krauss Bros. Lumber Co.* v. *Louis Bossert & Sons,* 62 F.2d 1004, 1006 (2d Cir. 1933) (L.Hand, J.); *Metro Industrial Painting Corp.* v. *Terminal Construction Co.,* 287 F.2d 382, 384 (2d Cir.), *cert. denied,* 368 U.S. 817 (1961); *Pock* v. *New York Typographical Union No. 6,* 223 F.Supp. 181, 183 (S.D.N.Y. 1963); *Victorias Milling Co.* v. *Hugo Neu Corp.,* 196 F.Supp. 64, 69-70 (S.D.N.Y. 1961); *Local 1416* v. *Jostens, Inc.,* 250 F.Supp. 496, 499 (D.Minn. 1966); See Committee on Commerce, Trade & Commercial Law, *The United States Arbitration Act and its Application,* 11 *A.B.A.J.* 153, 154 (1925).

In the present case, there is diversity of citizenship inasmuch as Hamilton is a citizen of New York and Republic is a citizen of Texas.

v. *Terminal Construction Co., supra,* 287 F.2d at 388, n.3 (concurring opinion); *Sinva, Inc.* v. *Merrill, Lynch, Pierce, Fenner & Smith, supra,* 253 F.Supp. at 364.

Even under the more modern grouping of contracts choice-of-law rule applied by New York to contracts generally, See *Auten v. Auten,* 308 N.Y. 155 (1954), New York law would be applicable as almost all the significant contacts of the transaction were with New York,— where the ultimate insureds reside and where it was agreed arbitration was to take place.

Before § 2(b) of the McCarran-Ferguson Act could become operative, State law *applicable* to the present case must be invalidated, impaired or superseded by the Federal Arbitration Act. Because Texas law would not be applicable even if there were no Federal Arbitration Act, any impairment of the Texas Arbitration Statute would not pose a McCarran-Ferguson Act problem.

Nor is any New York law enacted for the purpose of regulating the business of insurance invalidated, impaired or superseded by the application to this case of the Federal Arbitration Act. The New York Arbitration Act—which is substantially similar to the Federal Arbitration Act—provides that written agreements to arbitrate existing and future controversies are valid and enforceable. N.Y.C.P.L.R. § 7501. Moreover, there is no prohibition against arbitrating disputes arising under contracts of reinsurance.

The only possible difference between the New York and Federal Arbitration Acts relevant to the instant case concerns the question of the arbitrability of a claim that the reinsurance agreement was fraudulently induced. Such an allegation is made by the respondent in paragraph 18 of its answer.

Under federal law, where there is a broad, separable arbitration provision and a party alleges fraud in the inducement of the contract generally—as opposed to fraud in the inducement of the arbitration clause itself—this issue is reserved for the arbitrators and not for the Court. *Prima Paint Corp.* v. *Flood &*

Conklin Mfg. Co., 388 U.S. 395, 403-404 (1967); *Robert Lawrence Co.* v. *Devonshire Fabrics, Inc.,* 271 F.2d 402, 410 (2d Cir. 1959), *cert. dismissed,* 364 U.S. 801 (1960); *El Hoss Engineering & Transport Co.* v. *American Independent Oil Co.,* 289 F.2d 346, 349 (2d Cir. 1961); *Petition of Kinoshita & Co.,* 287 F.2d 951 (2d Cir. 1961).

In New York, the law "is not entirely clear." *Prima Paint Corp.* v. *Flood & Conklin Mfg. Co., supra,* 388 U.S. at 400, n. 3. Most of the reported cases state that a claim of fraud in the inducement of the contract is an issue for the Court and not for the arbitrators. *Matter of Exercycle Corp.,* 9 N.Y. 2d 329, 334, 214 N.Y.S. 2d 353, 356 (1961); *Matter of Wrap-Vertiser,* 3 N.Y. 2d 17, 163 N.Y.S. 2d 639 (1957) (dictum). On the other hand, there is authority holding that, if the arbitration clause is sufficiently broad, the issue of fraudulent inducement of the contract is a question for the arbitrators. *Matter of M. W. Kellog Co.,* 9 App. Div. 2d 744, 192 N.Y.S. 2d 869 (1st Dep't 1959); *Fabrex Corp.* v. *Winard Sales Co.,* 200 N.Y.S. 2d 278 (N.Y.Co. 1960); *Matter of Amphenol Corp.,* 49 Misc. 2d 46, 266 N.Y.S. 2d 768 (N.Y.Co. 1965), *aff'd mem.,* 25 App. Div. 2d 497, 267 N.Y.S. 2d 477 (1st Dep't 1966).

If New York law allows the issue of fraud in the inducement of the contract to be arbitrated, there is no conflict with the Federal Arbitration Act. But even if New York law requires this particular issue to be judicially resolved, there is no McCarran-Ferguson Act problem. The New York law on arbitrability is not specifically directed to the insurance business; nor is it intended to proscribe or permit "certain conduct on the part of insurance companies." *California League of Independant Insurance Producers* v. *Aetna Casualty & Surety Co.,* 175 F.Supp. 857, 860 (S.D.Cal. 1959). It follows that the New York law on arbitrability cannot be considered a state law enacted for the purpose of regulating the business of insurance within § 2(b) of the McCarran-Ferguson Act. In fact (as noted earlier in this

opinion), the purpose and scope of the McCarran-Ferguson Act have been narrowly construed; and federal law has been applied even where there is conflicting state law applicable to the business of insurance. *Maryland Casualty Co.* v. *Cushing, supra,* 374 *{sic}* U.S. 409 (Federal Maritime Law not rendered inapplicable by Louisiana direct action statute permitting certain suits against insurance companies); *Sears Roebuck & Co.* v. *All States Life Insurance Co., supra,* 246 F.2d 161 (Lanham Act not displaced by Texas Insurance Code provision requiring approval of the names of insurance companies by the Texas Board of Insurance Commissioners and a finding that such names were not likely to mislead the public.).

This Court holds that the McCarran-Ferguson Act presents no barrier to applying the Federal Arbitration Act to the present case. The respondent's cross-motion to dismiss the petition herein for lack of subject matter jurisdiction is denied.

II

This Court next considers the respondent's claim that the petition should be dismissed because the Court lacks in personam jurisdiction. This contention is without merit.

A foreign defendant's agreement to arbitrate in New York constitutes a submission to the jurisdiction of this Court to compel arbitration pursuant to § 4 of the Federal Arbitration Act. This was the holding in *Farr & Co.* v. *Cia Intercontinental de Navegacion,* 243 F.2d 342, 347 (2d Cir. 1957). Accord: *Victory Transport Inc.* v. *Comisaria General,* 232 F.Supp. 294, 295 (S.D.N.Y. 1963), *aff'd* 336 F.2d 354, 363 (2d Cir. 1964).

The arbitration agreement herein provides that arbitration shall "be held in the city where the home office of Ceding Company [Hamilton] is domiciled." (Article XII of Reinsurance Agreement). Hamilton, the petitioner, is a New York corporation, whose principal place of business is in New York City. (Petition To Compel Arbitration, ¶1). Under the rule enunciated in *Farr & Co.,* it is clear that, by agreeing to arbitrate in New York,

the respondent must be deemed to have consented to the jurisdiction of this Court to compel such arbitration.

The respondent further argues that the service of process effectuated in this case is a nullity because the respondent was not served within the territorial limits of the State of New York as required by Rule 4(f)[4] of the Federal Rules of Civil Procedure. The respondent was personally served at its home office in Dallas, Texas by the United States Marshal. In addition, the respondent was served by certified mail, return receipt requested, on December 14, 1967. (See Affidavit of Alfred Miller, sworn to March 14, 1968, p.2.).

In *Farr & Co.* v. *Cia Intercontinental de Navegacion, supra,* 243 F.2d 342, 348, the Court rejected the identical contention and upheld the sufficiency of service by registered mail. The Court stated that § 4 of the Federal Arbitration Act incorporates Rule 4(d)(7)[5] of the Federal Rules of Civil Procedure and

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[4] Rule 4(f) of the Federal Rules of Civil Procedure provides:

"(f) *Territorial Limits of Effective Service.* All process other than a subpoena may be served anywhere within the territorial limits of the state in which the district court is held, and, when authorized by a statute of the United States or by these rules, beyond the territorial limits of that state. In addition, persons who are brought in as parties pursuant to Rule 13(h) or Rule 14, or as additional parties to a pending action pursuant to Rule 19, may be served in the manner stated in paragraphs (1)-(6) of subdivision (d) of this rule at all places outside the state but within the United States that are not more than 100 miles from the place in which the action is commenced, or to which it is assigned or transferred for trial; and persons required to respond to an order of commitment for civil contempt may be served at the same places. A subpoena may be served within the territorial limits provided in Rule 45."

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[5] Rule 4(d)(7) of the Federal Rules of Civil Procedure provides:

"(7) Upon a defendant of any class referred to in paragraph (1) or (3) of this subdivision of this rule, it is also sufficient if the summons and complaint are served in the manner prescribed by any statute of the United States or in the manner prescribed by the law of the state in which the district court is held for the service of summons or other like process upon any such defendant in an action brought in the courts of general jurisdiction of that state."

permits State methods of serving process to be used to compel specific performance of arbitration agreements. Rule 4(f) which relates solely to federal service of process was held not to bar the use of State methods of service, pursuant to Rule 4(d)(7). Applicable New York law holds that "consent to jurisdiction includes consent to service by any method consistent with due process." *Petrol Shipping Corp.* v. *Kingdom of Greece,* 360 F.2d 103, 107 (2d Cir.), *cert. denied,* 385 U.S. 931 (1966). Service of process in the present case is unquestionably valid under New York law.

The respondent's cross-motion to dismiss for lack of in personam jurisdiction is denied.

III

The respondent also seeks to dismiss the petition on the ground that the petitioner has failed to join an indispensable party. The respondent asserts that the reinsurance agreement entered into in September, 1965 was actually tripartite in nature and "was evidenced in part by two separate agreements," one between the petitioner and the respondent and the other between the respondent and Financial Security Life Insurance Company. (Affidavit of Thomas G. Nash, Jr., sworn to March 11, 1968, p.2.). By the terms of this tripartite agreement, the petitioner would cede to the respondent 80% of the risks written, provided that the respondent would cede 80% of that amount to Financial Security Life Insurance Company. (Affidavit of William A. Boles, sworn to January 3, 1968, p.1, attached as Exhibit A to Nash Affidavit.). Moreover, there was no arbitration agreement entered into between the three parties. (Boles Affidavit, p.2.). Because Financial Security is not a party in this proceeding, the respondent asserts "it is improper to pursue an action to construe this contract when only two of the three parties affected by the ultimate resolution of the issues are within the jurisdiction and participating in these proceedings." (Respondent's Memorandum of Law, p.12.).

The respondent's contention that the reinsurance agreement is actually tripartite in nature is flatly contradicted by the affidavit of Edwin S. Newman, who was present at the time of the contract negotiations. In his affidavit (sworn to January 19, 1968), Mr. Newman avers that "[t]he reinsurance agreement of September 1965 between Hamilton Life Insurance Company and Republic National Life Insurance Company was a separate and distinct agreement between the parties, and there was no concurrent 'parol' agreement apart from said actual reinsurance treaty that the group business reinsured from Hamilton Life to Republic National Life was in turn to be reinsured to a third company [Financial Security] . . ." (p.2).

Moreover, the Hamilton-Republic reinsurance agreement provides:

"ARTICLE XIV AMENDMENT

This instrument contains the sole agreement between the parties hereto on the subject of group reinsurance, and it may be amended only by an instrument in writing which expresses such an intention and is signed with the same formalities as this instrument."

The respondent, Republic, has not produced any writing evidencing the so-called tripartite agreement. To allow the respondent to prove that there was an oral agreement modifying the Hamilton-Republic reinsurance agreement would be contrary to the express terms of the agreement and violative of the parol evidence rule. See, *Fogelson* v. *Rackfay Construction Co.,* 300 N.Y. 334, 340 (1950).

In any event, Financial Security is not an indispensable party to the present proceeding, which is brought not to construe the parties' rights under the reinsurance agreement, but only to enforce the Hamilton-Republic agreement to arbitrate.

The contention that there is no tripartite arbitration agreement joined in by all of the alleged parties—the petitioner (Hamilton), the respondent (Republic) and Financial Security—does not prevent enforcement of the Republic-Hamilton arbitration agreement.

The crucial fact is that the petitioner and the respondent agreed to arbitrate disputes between themselves. There is no impediment to enforcing an agreement to arbitrate entered into between less than all of the parties to a dispute. *Wilko* v. *Swan,* 201 F.2d 439, 445 (2d Cir.), *rev'd on other grounds,* 346 U.S. 427 (1953); *Lumbermen's Mutual Casualty Co.* v. *Borden Co.,* 268 F. Supp. 303 (S.D.N.Y. 1967). Whatever claims the respondent may have against Financial Security for indemnification or otherwise do not prevent enforcement of the petitioner's right to compel arbitration under the reinsurance agreement.

The respondent's cross-motion to dismiss for failure to join an indispensable party is denied.

IV

The Court concludes that there is no *bona fide* question as to the making and validity of the arbitration agreement and the respondent's "failure to comply therewith." The parties are, therefore, ordered to proceed to arbitration in accordance with the terms of the agreement.

The arbitration clause in the present case is separable from the rest of the agreement and clearly broad enough to cover the defenses raised in the respondent's answer: fraud in the inducement of the contract generally, lack of consideration, failure to comply with conditions precedent, illegality of the subject matter of the contract and breach of contract. Indeed, "it would be hard to imagine an arbitration clause having greater scope than the one before us." *Robert Lawrence Co.* v. *Devonshire Fabrics, Inc., supra,* 271 F.2d at 412. The validity of these claims as well as the question of the respondent's liability to the petitioner will, therefore, be determined by the arbitrators.

The respondent's alternative request that these proceedings be stayed is denied because it has "not made out a clear case of hardship or inequity in being required to go forward . . ." *Landis* v. *North American Co.,* 299 U.S. 248, 254-255 (1936). A stay of these proceedings would "work damage" to the petitioner,

which has been unsuccessfully attempting to compel arbitration of this dispute for almost one year. Moreover, similar requests that proceedings in this district be stayed have recently been denied by the United States District Court for the District of Arizona, the Ninth Circuit Court of Appeals and the United States Supreme Court. In fact, proceedings in the United States District Court for the District of Arizona have been stayed pending this Court's determination of the motions before it.

The petitioner's motion to compel arbitration is granted. The respondent's cross-motion to dismiss the petition or, in the alternative, to stay these proceedings is denied.

Settle order on notice in accordance with the views expressed in this opinion.

Dated: New York, N. Y.
July 30, 1968.

WILLIAM B. HERLANDS
U. S. D. J.